Defense Acquisition University

Multi-Year Strategizing, Planning and Contracting

Presented by:
John Krieger (703) 805-5046
John Pritchard (703) 805-3800

Agenda

- FAR Guiding Principles
- Definitions
- Multi-year Contracting (MYC)
  - Description
  - Types of Multi-year Contracting (MYC)
    - Economic Order Quantity (EOQ)
    - Non-Economic Order Quantity (Non-EOQ)
  - Requirements for MYC
  - Four Interlaced Parallel Processes
  - MYC Basic Funding Rules
  - Multi-year Cancellations/Sequence of Events
    - Building Cancellation Estimates

FAR Guiding Principles

FAR 1.102(d) The role of each member of the Acquisition Team is to exercise personal initiative and sound business judgment in providing the best value product or service to meet the customer's needs. In exercising initiative, Government members of the Acquisition Team may assume if a specific strategy, practice, policy or procedure is in the best interests of the Government and is not addressed in the FAR nor prohibited by law (statute or case law), Executive order or other regulation, that the strategy, practice, policy or procedure is a permissible exercise of authority.

Use the rules to say Yes,

Multi-year Contracting (MYC) Definitions

- **"Multi-year contract" (MYC) means a contract for the purchase of supplies or services for more than 1 year, but not more than 5 years.**
  - **A MYC may provide that performance under the contract during the second and subsequent years is contingent upon the appropriation of funds, and (if it does so provide) may provide for a cancellation payment to be made to the contractor if appropriations are not made.**
  - **Key distinguishing difference between multi-year contracts and multiple year contracts is that multi-year contracts buy more than 1 year's requirement (of a product or service) without establishing and having to exercise an option for each program year after the first.**

Multi-year Contracting (MYC) Definitions

- "**Cancellation**" means the cancellation (within a contractually specified time) of the total requirements of all remaining program years.
- "**Cancellation charge**" means the amount of unrecovered costs which would have been recouped through amortization over the full term of the contract, including the term canceled.
- "**Cancellation ceiling**" means the maximum cancellation charge that the contractor can receive in the event of cancellation.

Multi-year Contracting (MYC) Definitions

- "**Nonrecurring costs**" means those costs which are generally incurred on a one-time basis and include such costs as plant or equipment relocation, plant rearrangement, special tooling and special test equipment, preproduction engineering, initial spoilage and rework, and specialized work force training.

- "**Recurring costs**" means costs that vary with the quantity being produced, such as labor and materials.

Multi-year Contracting (MYC) Objectives FAR 17.105-2

Use of MYC is encouraged to take advantage of the following:

- **Lower costs.**
- **Enhancement of standardization.**
- **Reduction of administrative burden in the placement and administration of contracts.**
- **Substantial continuity of production or performance, thus avoiding annual startup costs, preproduction testing costs, make-ready expenses, and phase-out costs.**
- **Stabilization of contractor work forces.**

Multi-year Contracting (MYC) Objectives FAR 17.105-2

- Avoidance of the need for establishing quality control techniques and procedures for a new contractor each year.
- Broadening the competitive base with opportunity for participation by firms not otherwise willing or able to compete for lesser quantities, particularly in cases involving high startup costs.
- Providing incentives to contractors to improve productivity through investment in capital facilities, equipment, and advanced technology.

Multi-year Contracting (MYC)

- **Special contracting method for acquiring known requirements for more than one year (but NTE five years) even though subsequent years funding isn't available at time of award**
- **Allows the contractor to conduct production and capitalization planning in a more efficient manner**
- **In event of a contract cancellation, contractor shall be paid the "Cancellation Charge" for loss of costs which would have been recouped on a fully funded contract for all requirements**
- **"Cancellation Charges" and are limited to preaward negotiated (not to exceed) ceilings**

Multi-year Contracting (MYC)

- **Under MYC Congress formally acknowledges planned major procurement(s) of a stated period (up to 5 years) which strongly influences future congressional appropriations**

- **If congress fails to appropriate future funds, the future years requirements are cancelled and the contractor is entitled to costs that the contractor can’t amortize due to the lost production**

PRINCIPAL DIFFERENCES BETWEEN CONVENTIONAL AND MULTI-YEAR CONTRACTS

	ANNUAL-BUY	MULTI-YEAR
Initial Contract	One contract for the FY 1 requirement of 20 flying saucers	One multi-year contract for all 100 flying saucers
Congressional Commitment	To FY 1 buy of 20 flying saucers	To total buy of 100 flying saucers from FY 1 through FY 5
Treatment of out-year requirements in the initial contract	Option for each fiscal year's requirements	Separate line item for each fiscal year's requirements
Required to "activate" contract commitment to buy the next year's requirements*	1) Same quantity authorization as was provided for in FY 2 option 2) Annual appropriation by Congress adequate to fund FY 2 of the option 3) Contracting Officer determines that exercising the option is the best method of fulfilling the Government's need, price and other factors considered	Annual appropriation by Congress adequate to fund FY 2 of the multi-year contract
Contractual action required to "activate" commitment to buy the next year's requirements*	Contract modification to exercise FY 2 option	Contract modification obligating funds for FY 2 requirements

* Note that these differences are relevant to each of the out-years: FY 2, FY 3, FY 4, and FY 5

Types of MYC

- **Non-Economic Order Quantity (NEOQ)**
  - **Example is the recommendation to purchase 100 units requesting funds for the first 20 units (year 1 units) and authority to purchase the 80 out year units**
  - **Congress not bound to appropriate years 2-5,**
    - **if it isn't funded, the Government pays a cancellation charge to the contractor (up to the "cancellation ceiling" identified by year)**
  - **Advantage of Non-EOQ is that it can acquire the 100 units at lower costs because it avoids annual startup costs and provides longer planning for setting up production equipment and processes**

Types of MYC

- **Economic Order Quantity (EOQ)**
  - **Program would be budgeted in advance with Procurement funds for the entire 100 units, but only provided the funds for the first year (the first 20 units)**
    - **Remaining funds would be requested each year for 2-5**
  - **Congressional prerogatives for future funding is the same as Non-EOQ, but cancellation ceilings are higher under this arrangement due to up-front investments in material and labor throughout the EOQ purchases.**
  - **Used to obtain purchases with lower prices**

Requirements for a Multi-year Contract (FAR 17.1)

- **For DoD, the HCA may enter into a multi-year contract for supplies if—**
  - **MYC will result in substantial savings**
  - **Minimum need to be purchased is expected to remain substantially unchanged (production rate, procurement rate, and total quantities)**
  - **A stable design and the technical risks are not excessive**
  - **Reasonable expectation that, throughout the contract period, the HCA will request future funding at a level to avoid contract cancellation; and**
  - **The estimates of both the contract cost and the cost avoidance through the use of a multi-year contract are realistic.**

Congress traditionally looks for > 10% savings
storically, anything less was in the estimation “noise
owever, Congress has recently approved > 5% saving

Initiation of a Multi-year Program

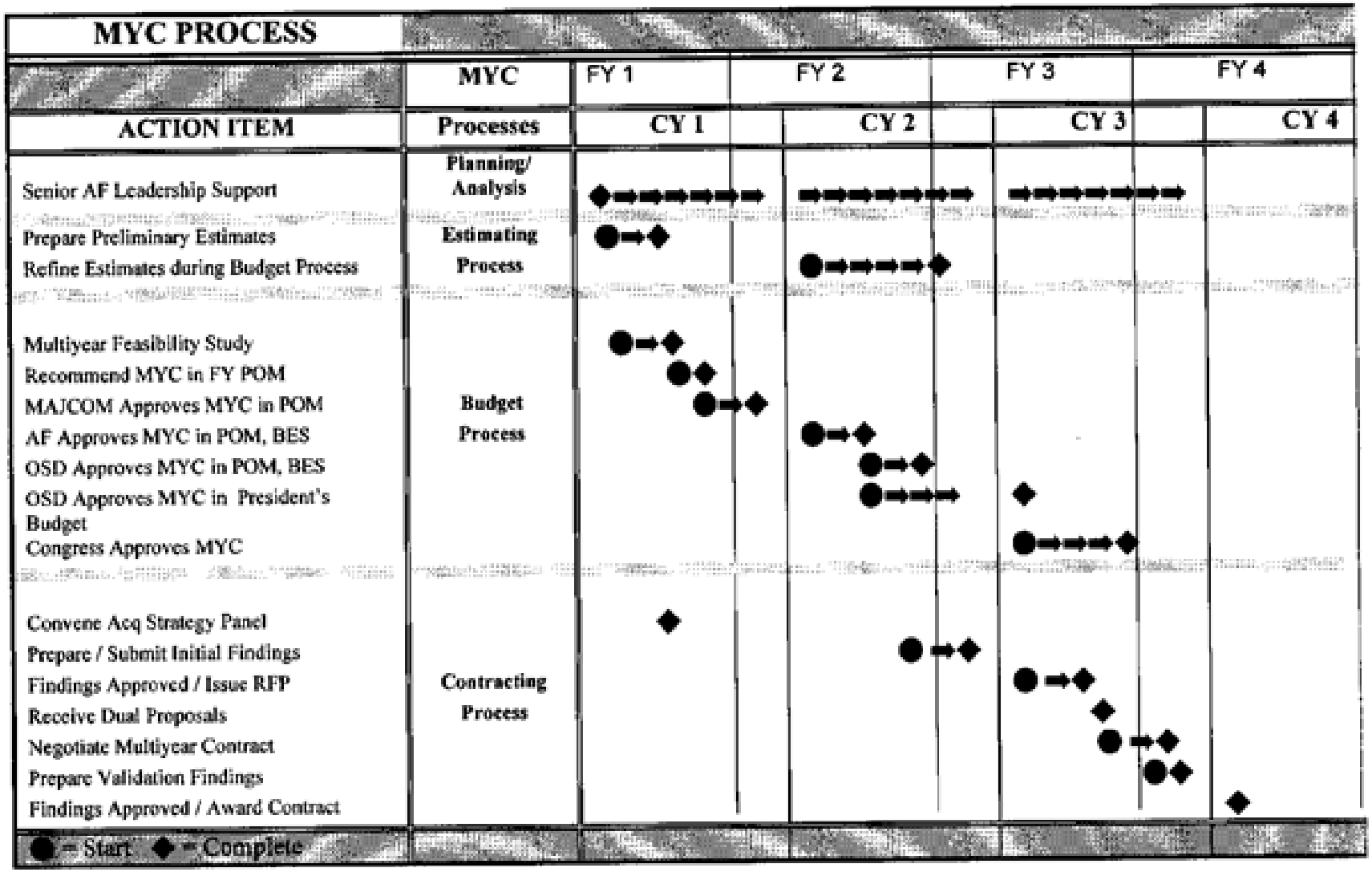
- **Either by nomination from the Service/Department or specifically authorized/appropriated by law**
  - **DoD submits a MYP to Congress through the President's Budget and with a legislative language request.**
    - **If approved by Congress, the MYP will usually be authorized in the Authorization and Appropriation's Acts.**
  - **If Congress initiates the MYP by providing Authorization and Appropriations language in a law, even though DoD did not nominate the program, all statutes and regulations remain**

Four Interlaced Parallel Process

(AF MYC Informational Guide)

- **Planning**
  - **Prepare preliminary planning estimates to support feasibility estimates**
    - Conventional Cost Estimates vs. Multi-year Cost Estimates
    - Directly feeds data into feasibility analysis which is done in parallel
    - Contractor is usually best source (competitive MYC will have additional challenges)
- **Analysis**
  - Is MYC logical and sufficient benefit to your program
    - Acquisition Strategy
- **Estimating Budget**
  - Recommend MYC (if appropriate) in the Program Objective Memorandum (POM)
  - Approval of the Recommended Multi-year Contract in the POM
  - Refine Estimates (old POM estimates will now be a year old)
  - Approval of the Recommended Multi-year Contact in the BES
  - Prepare Initial Multi-year Findings
  - Approval of the Multi-year Contract in the President's budget
- **Contracting**
  - Obtain Approval (via review cycle) of Initial Multi-year Findings and Issue RFP
  - Receive dual proposals (Conventional Proposal and Multi-year Proposal)
  - If appropriate savings, obtain Congressional Approval of Recommended MYC
  - Negotiate Multi-year Contact
  - Prepare Validation Findings (price and other negotiated terms to validate findings)

MYC Process



(AF MYC Guide)

LEVEL UNIT PRICING VS. VARIABLE UNIT PRICING

- **"Level Unit Pricing" means all items under the multi-year contract have identical unit prices. Level unit prices result from amortizing certain costs over the entire contract quantity. These costs include nonrecurring costs. In major systems acquisitions, these costs can also be those recurring or variable costs that are not alike from item to item or program year to program year**

- **"Variable Unit Pricing" means that unit prices may vary from unit to unit or from program year to program year. In major systems acquisitions, the actual cost of production items tends to vary (usually downward, as the system matures and more units are produced). Consequently, variable unit pricing is the norm for major system MYCs and provides the only way to ensure that unit prices reflect item value.**

Pricing Options

PROGRAM YEAR	Y2	Y3	Y4	Y5	TOTAL
PROGRAM QUANTITY	10	10	10	10	10	50
LEVEL UNIT PRICING	$1000	$1000	$1000	$1000	$1000	$5000
VARIABLE UNIT PRICING	$1200	$1100	$1000	$900	$800	$5000

Rules Governing Funding of MYCs

- **Preparation and Submission of Budget Estimates (OMB Circulars A-11), Instructions on Budget Execution (A-34), funded one year at a time with annual appropriations.**
- **General funding rules for each year of MYC are:**
  - **Fully fund the end items being procured**
  - **Fund at least the termination liability of the advance (i.e., EOQ and Long Lead) procurement**
  - **Fund at least the recurring cost portion of the cancellation ceiling**
  - **Estimates should be based on prior history for the same or similar items or proven cost estimating techniques**
  - **With the exception of funding for EOQ procurement and advance procurement for long lead-time items as defined in DoD 7000.14-R, Volume 2A, section 010202, multi-year procurement contracts should comply with full funding.**
    - **10 USC 2306b(h)(2) authorizes multi-year contracts to be used for "advance procurement of components, parts, and materials necessary to the manufacture of a weapon system" (i.e., long lead procurement) and for "advance procurement ... in order to achieve economic lot purchases and more efficient production rates" (i.e., EOQ procurement).**

Multi-Year Contract Cancellations

- **Cancellation clauses provide an agree-upon method for ending the contract**
  - **Except for the first period, all other periods are subject to cancellation**
- **Under a multi-year contract, the failure to provide funds for out-year units would result in a “cancellation” of those years of effort**
  - **contractor must deliver the units for the years funded**
  - **Multi-year contract provides for cancellation at the times when funding is required for out-years in accordance with contract procedures**

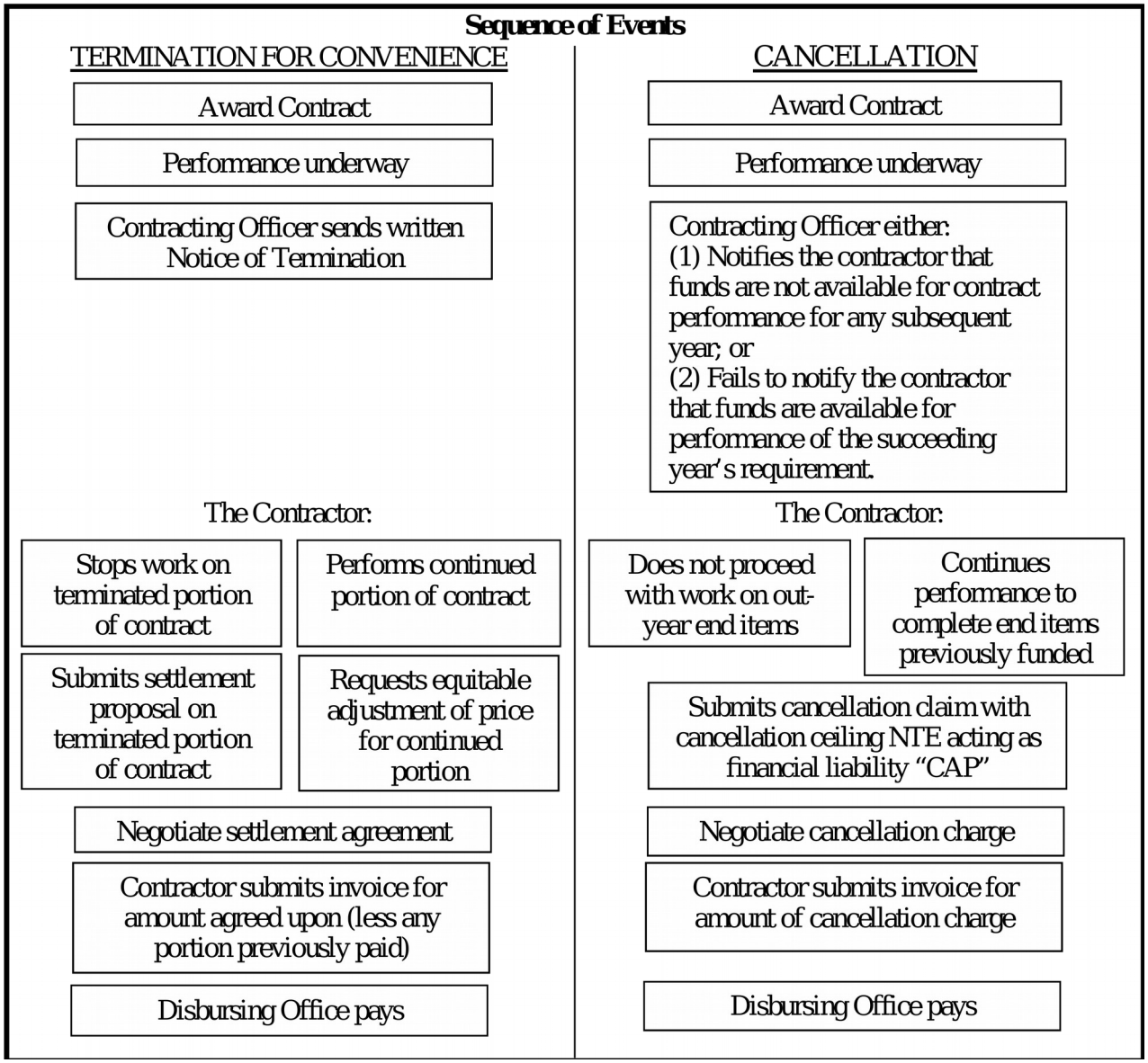
Multi-Year Contract Cancellations

- **Conventional Contract - a decision not to award option or a termination for convenience would normally occur if Congress fails to provide appropriate funds**
- **Multi-Year Contract provides for “cancellation” when future appropriations are not made**
- **The cancellation clause (FAR 52.217-2 Cancellation Under Multiyear Contracts) contains rules for ending the contract**
  - **Except for the first period, all other periods are subject to cancellation**
- **MYCs are also subject to T4C and T4D**

Termination vs. Cancellation

	Termination for Convenience	Cancellation
Conventional Annual Buy Contracts	Yes	No
Multi-year Contracts	Yes	Yes
When the Action May Be Taken	Anytime during the life of the contract	Anytime, but usually at the start of a fiscal year
What the Action Affects	Either the total contract quantity or a portion of it, as indicated in the termination notice	All subsequent fiscal years' quantities
Reason the Action Is Taken	The Contracting Officer determines a termination is in the Government's interest	Funds are not available for contract performance for the succeeding fiscal year
Authority for the Action	"Termination for Convenience of the Government" (Fixed Price) clause at FAR 52.249-2	"Cancellation Under Multi-year Contracts" clause at FAR 52.217-2
Termination Liability	As negotiated	As negotiated but NTE cancellation ceiling "CAP"

Termination vs. Cancellation


Sequence of Events
TERMINATION FOR CONVENIENCE
Award Contract
Performance underway
Contracting Officer sends written Notice of Termination
The Contractor:
Stops work on terminated portion of contract
Performs continued portion of contract
Submits settlement proposal on terminated portion of contract
Requests equitable adjustment of price for continued portion
Negotiate settlement agreement
Contractor submits invoice for amount agreed upon (less any portion previously paid)
Disbursing Office pays
CANCELLATION
Award Contract
Performance underway
Contracting Officer either:
(1) Notifies the contractor that funds are not available for contract performance for any subsequent year; or
(2) Fails to notify the contractor that funds are available for performance of the succeeding year's requirement.
The Contractor:
Does not proceed with work on out-year end items
Continues performance to complete end items previously funded
Submits cancellation claim with cancellation ceiling NTE acting as financial liability "CAP"
Negotiate cancellation charge
Contractor submits invoice for amount of cancellation charge
Disbursing Office pays

Building a Cancellation Ceiling Estimate

(AF MYC Guide)

1. Decide what costs can be included in the cancellation charge
2. Establish the points in time when the contract could be cancelled
3. Evaluate the task of estimating a cancellation ceiling
4. Estimate the nonrecurring cost incurred but not recovered
5. Estimate the nonrecurring costs the contractor is committed to incur
6. Estimate the recurring cost incurred for the canceled end items
7. Estimate the recurring costs the contractor is committed to incur for the cancelled end items
8. Assess the impact cancellation could have on the cost of end items already purchased
9. Consider the offset potential of the work in process on the canceled end items
10. Consider the offset potential of cancelable commitments
11. Sum up the results of steps four through ten

Building a Cancellation Ceiling Estimate

(AF MYC Informational Guide)

Of Year _____ of the Multi-year Contract

BUILDING BLOCKS	ESTIMATE	RESULTING FROM STEP
Nonrecurring Costs incurred but not yet recovered	$	Four
Nonrecurring Costs the contractor is committed to incur	+	Five
Recurring Costs incurred for the canceled end items	+	Six
Recurring costs the contractor is committed to incur for the canceled end items	+	Seven
The impact of the cancellation on the cost of the end items already purchased (i.e., those not canceled)	+ _____	Eight
SUBTOTAL >>>>	$	
OFFSETS		
Work in process on the canceled end items that can either be delivered to the Government or sold	less _____	Nine
SUBTOTAL >>>>	$	
Commitments the contractor has made that can be canceled in whole or in part	less _____	Ten
TOTAL >>>>	$	Eleven

Figure 6.A

PREPARE A MULTI-YEAR JUSTIFICATION PACKAGE (AF Multi-Year Information Guide)

Exhibit MYP-1, Multi-year Procurement Criteria (DoD 7000.14-R, Volume 2B, Chapter 4)
Program: _____

1. **Multi-year Procurement Description.**
2. **Benefit to the Government.**
   a. Substantial Savings
   b. Stability of Requirement
   c. Stability of Funding
   d. Stable Configuration
   e. Realistic Cost Estimates
   f. National Security
3. **Source of Savings** $ in Millions

   Inflation
   Vendor Procurement
   Manufacturing
   Design/Engineering
   Tool Design
   Support Equipment
   Other
   Total
4. **Advantages of the MYP**
5. **Impact on Defense Industrial Base**
6. **Multi-year Procurement Summary** Annual Contracts Multi-year Contract

   Quantity
   Total Contract Price
   Cancellation Ceiling (highest point)
   Funded
   Unfunded
   $ Cost Avoidance Over Annual
   % Cost Avoidance Over Annual

References/Sources

- **10 USC 2306b Multiyear contracts: acquisition of property authorizes HCAs to enter into MYC when appropriate**
- **FAR Subpart 17.1 Multiyear Contracting and the supplements in the DFARS/PGI**
- **Pub. Law 105-85 § 806 Multiyear procurement contracts**
- **DoD 7000.14 Department of Defense Financial Management Regulations (FMRs)**
- **AF Multi-Year Informational Guide**

Discussion/Questions